ARIF HABIB LIMITED

REP-300

Pakistan Budget FY25 Preview
Fiscal prudence during IMF negotiations

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AHL Research

D: +92 21 32462742

UAN: +92 21 111 245 111, Ext: 322

F: +92 21 32420742

E: ahl-research@arifhabibltd.com

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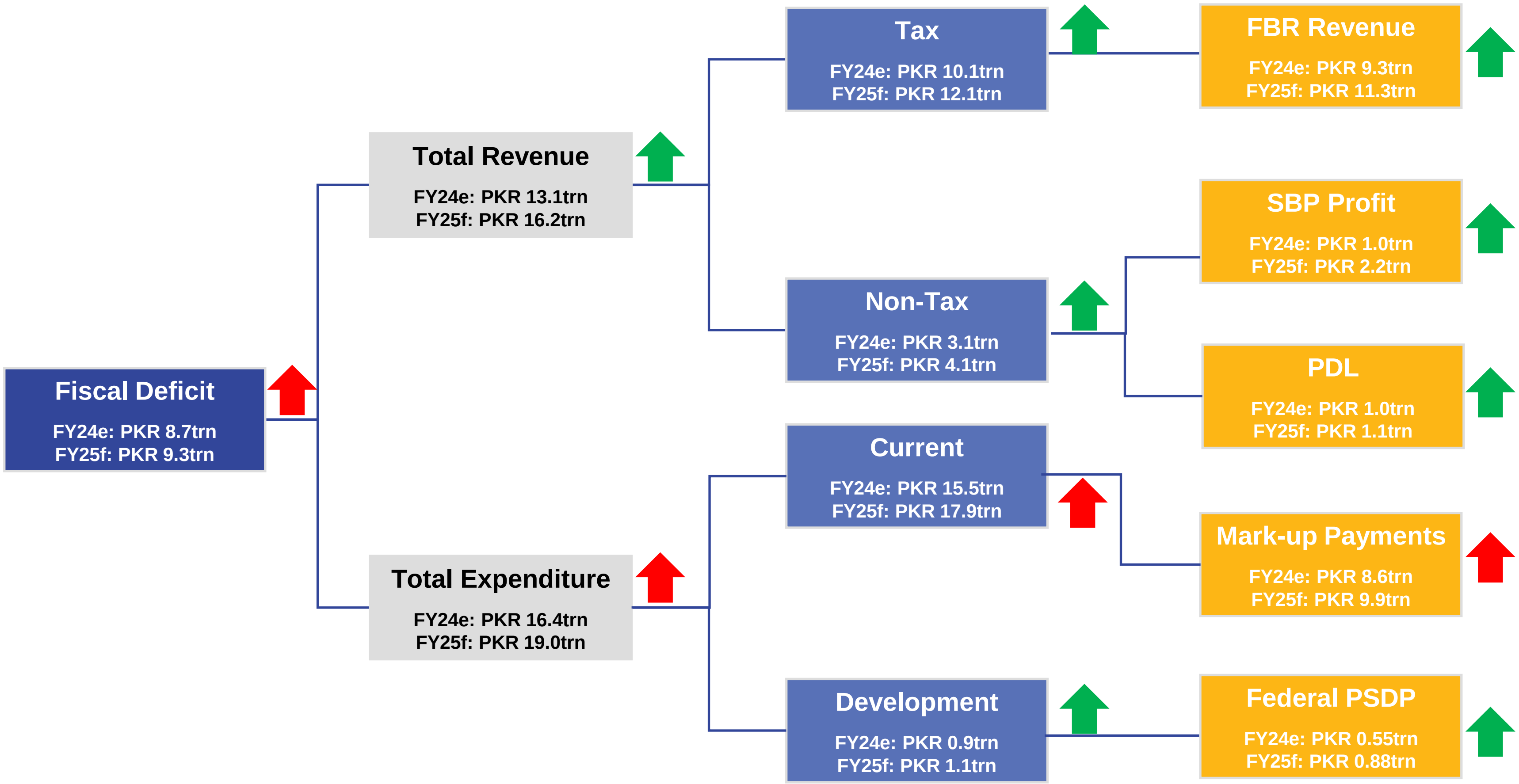

Source (s): AHL Research Estimates

Budget Preview FY25 Blueprint

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1

Pakistan to unveil FY25 budget amid IMF talks

Pakistan is scheduled to present its federal budget for FY25 on 7th Jun'24. Alongside this, the government will be negotiating a long-term Extended Fund Facility (EFF) program with the IMF in June, involving a package amounting to USD 7-8bn.

2

FBR's tax collection targets

The Federal Board of Revenue (FBR) aims to broaden the tax base in the FY25 budget by targeting the untaxed sectors/industries and various approaches. The FBR's target for revenue collection is expected to be PKR 12.4trn.

3

Non-tax revenue projections

Government expects non-tax revenue collection to increase to PKR 3.5trn in FY25 with major contribution expected from State Bank's profits and Petroleum Development Levy (PDL).

4

Current expenditure scaled up

Current expenditure in FY25b is anticipated to swell up to PKR 16.7trn against FY24's budgeted current expenditure of PKR 13.3trn mainly due to higher markup payments.

5

PSDP expenditure anticipated to rise

Federal Public Sector Development Program expenditure is projected to climb from FY24's budgeted figure of PKR 0.95trn to PKR 1.0trn in FY25b.

6

Fiscal deficit

Fiscal deficit in FY25b projected by government is PKR 9.3trn. We anticipate the fiscal deficit to arrive at PKR 9.4trn. The increase in fiscal deficit is primarily due to increase in current expenditure followed by increase in development expenditure.

7

Key revenue measures

Key revenue measures include bringing more individuals under the tax net by targeting the agriculture, retail, and wholesale sectors. In addition to this, the imposition of GST/carbon tax or hike in PDL on MS and HSD are also anticipated during FY25 budget.

8

Economic projections

GDP growth is rebounding significantly and is projected at 4% in FY25b. Inflation is also anticipated to witness a significant decline, to arrive at 12%. Additionally, the current account deficit is expected to arrive at USD 4.2bn.

9

Sector summary

Gainers: Cement, Steel

Neutral: Banks, Automobile assemblers, Textile, Tech

Steady performers: Fertilizer, Power, E&Ps and OMCs.

10

Budget FY25 aligning with IMF conditions

Budget FY25 is expected to remain neutral and balanced, adhering closely to the criteria outlined by the International Monetary Fund (IMF).

Budget Preview FY25
Steering towards growth amid IMF negotiations

- Set against a backdrop of relative economic steadiness, Pakistan's forthcoming budget for FY25 arrives amidst some positive economic developments.
- Key indicators show improvement, with GDP growth rebounding significantly from -0.2% in FY23 to a projected 2.38% for FY24. Inflation is also moderating, anticipated to decline from 29% in FY23 to 24.2% in FY24. Additionally, the current account deficit is narrowing, expected to decrease from -1% of GDP in FY23 to -0.1% in FY24. Corporate performance has remained robust, further supporting this optimistic outlook.
- However, concerns remain regarding subdued consumption demand due to strict macroeconomic policies, sluggish private investment, and global economic uncertainties. Most importantly, securing a larger International Monetary Fund (IMF) program of around USD 7-8bn is essential.
- It will be interesting to witness how the government navigates through the challenges of managing potential IMF conditions, grappling with colossal debt servicing, and ensuring the continued improvement of tax revenue collection. However, while the immediate focus may understandably lean towards short to medium-term solutions, there is a resounding call for a shift towards a more holistic, long-term approach.
- Thus, this year's budget holds key significance, as it will set the policy direction needed for sustained economic growth while ensuring Pakistan can secure vital IMF support.
- In anticipation of the budgetary proposals, stakeholders are clamoring for measures that prioritize sustainable growth and development. This includes substantial investments in human capital and technology, alongside structural reforms aimed at bolstering efficiency and overall economic performance. The establishment of the Special Investment Facilitation Council (SIFC) underscores a commitment to fostering private sector engagement, while the privatization of underperforming enterprises is seen as a step towards streamlining the state's fiscal obligations.

Exhibit: Economic and budgetary targets

Item		FY24e	FY25b
Key economic targets			
GDP growth	%	2.4	3.7
Inflation	%	24.1	11.8
Fiscal deficit	% of GDP	8.1	7.5
Current account balance	USD bn	1.8	4.2
Key budgetary targets			
FBR revenue	PKR trn	9.3	12.4
Mark-up payments	PKR trn	8.6	9.8
Federal PSDP	PKR trn	0.6	1.0
Defense	PKR trn	1.8	2.2

Source (s): News Reports, AHL Research

Budget Preview FY25
Steering towards growth amid IMF negotiations

- Moreover, there is a pressing need to address the issue of untaxed segments of society, while simultaneously broadening the tax base to enhance revenue streams.
- By doing so, the government can mitigate the necessity for deficit financing, thereby alleviating the burden on future budgets.
- Additionally, a re-evaluation of tight monetary policy and concerted efforts to reduce the stock of debt are deemed imperative in creating fiscal space for future contingencies.
- While the impending budget may lean towards short-term needs, it is imperative that policymakers heed the call for a more forward-thinking, long-term approach.

Key takeaways:

- To sum up, as the government prepares to announce Budget FY25 on June 7th, 2024, it is strongly believed that **the fiscal discipline will take precedence over populist spending**.
- The upcoming budget, likely to be in line with IMF demands, **may lack 'significant' relief measures** for the public.
- It is expected that the upcoming budget will center on initiatives aimed at broadening the tax base, thereby **almost meeting revenue targets**.
- Efforts to **curtail overall expenditure** are also anticipated, particularly in light of the substantial portion of tax revenue dedicated to servicing markups, accounting for over 80%.
- Moreover, there is a concerted emphasis on **ensuring social protection** for vulnerable segments of society amidst these fiscal adjustments. This includes measures aimed at safeguarding the welfare of those most in need, all while **adhering to the targets likely to be set forth by the IMF** in the ongoing negotiation of a new program.

Budget Preview FY25
Navigating tight fiscal terrain

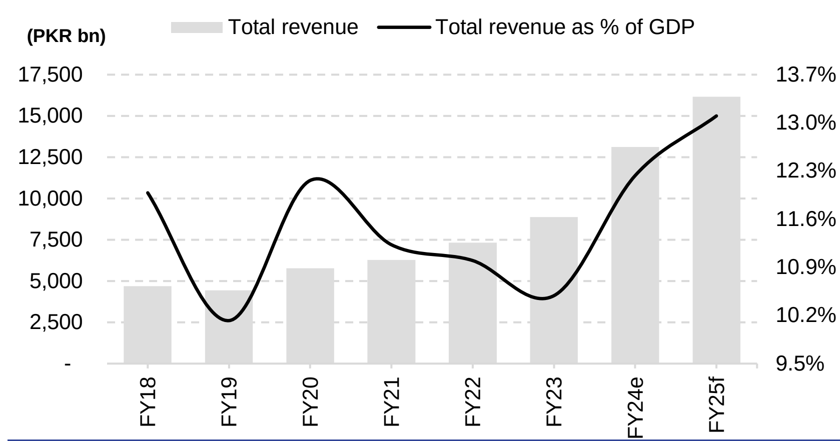
Revamping fiscal reforms to enhance revenue collection:

- Government plans to increase its gross revenue generation in FY25 budget to PKR 16.6trn. While, we expect the total revenue in FY25 to arrive at PKR 16.2trn.
- To bolster revenue generation, the government's budget strategy places a strong emphasis on tax reforms.
- It is anticipated that these efforts will include broadening the tax base by incorporating untaxed entities, treating agricultural income as regular income like any other sector, imposing higher taxes on non-filers and increasing their transaction costs, improving tax collection infrastructure, raising the Petroleum Development Levy (PDL), and introducing new taxes such as a carbon tax.

Revenue targets

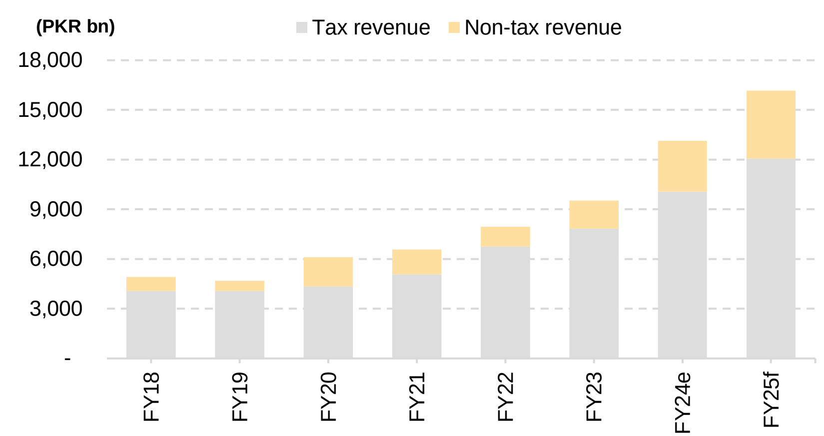
- We anticipate a 48% YoY growth in total revenue collection during FY24e to PKR 13.1trn (FY25b: PKR 16.6trn) from last year’s collection of PKR 8.9trn.
- This growth is primarily expected to come from tax revenue which is expected to post a jump of 29% YoY to PKR 10.1trn (FY25b: PKR 13.1trn).
- FBR’s collection is expected to clock-in at PKR 9.3trn by the end of FY24e while jumping up to PKR 11.2trn in FY25f.
- To achieve controlled economic growth, the government plans to impose significant taxes on under-taxed sectors and broaden the national tax base.
- Furthermore, the government is prepared to implement unpopular tax measures to meet this objective.
- Moreover, the government expects non-tax revenue collection to increase by 18% YoY to PKR 3.5trn in FY25b (FY24e: PKR 3.1trn).
- We believe, the non-tax revenue will majorly be contributed by SBP’s profit of about PKR 2.2trn (+126% YoY) and collection from PDL of PKR 1.1trn (+12% YoY).

Exhibit: Historical trend & projections of revenue collection



Source (s): MOF, AHL Research

Exhibit: Breakdown of revenue collection



Source (s): MOF, AHL Research

Navigating tight fiscal terrain

Mark-up payments- the main driver of current expenditure:

- Total expenditure is projected to reach 15.3% of GDP, amounting to PKR 16.4trn in FY24e and PKR 18.2rn in FY25b. This represents an annual increase of 45% YoY in FY24e and 27% in FY25b.
- The primary driver of total expenditure's growth will be current expenditure, anticipated to rise by 43% YoY, reaching PKR 15.5trn by the end of FY24e.
- The surge in current expenditure is mainly attributed to a significant increase in mark-up payment, expected to be PKR 8.6trn (+48% YoY), driven by higher interest rates. Although interest rates are expected to come down in FY25f, but with domestic borrowing anticipated to remain high, we don't expect any decline in markup payments in the next FY (FY25f: PKR 9.8trn).
- In contrast, during FY24e, development expenditure is expected to be around PKR 0.94trn, up from PKR 0.89trn.

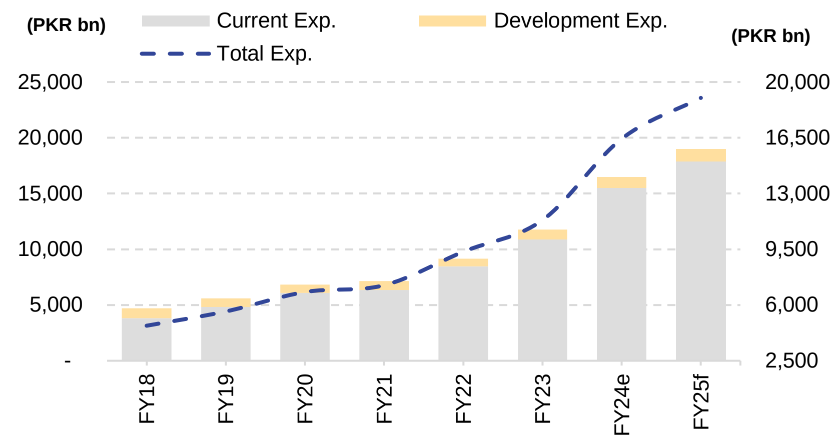
Conscious PSDP amid limited fiscal space:

- In FY24b, the government budgeted to spend about PKR 2.5trn in total PSDP (out of which 0.95trn was for federal and PKR 1.55trn was for provincial).
- Of the total federal amount ~PKR 507bn has been authorized till Apr'24, actual expenditure settled at PKR 353bn.
- In FY25 allocation for federal PSDP is budgeted to be ~PKR 1trn (a jump of 5.2% YoY), where we expect the utilization of the same would arrive at PKR 880bn. This surge in spending would stimulate economic growth in the economy.

Fiscal deficit expected to fall short of government projections:

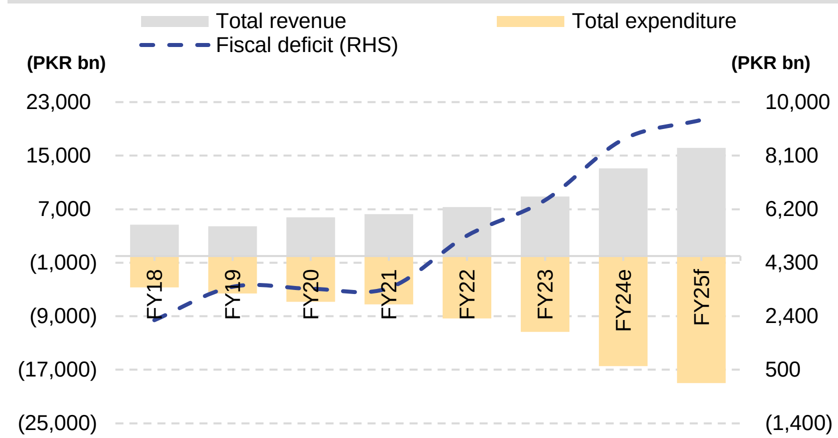
- Government is estimating a fiscal deficit of PKR 9.3trn (7.5% of GDP) in FY25b.
- We expect the fiscal deficit to be slightly higher than the government's estimates to clock at around PKR 9.4trn (7.6% of GDP) in FY25f.
- For FY24e, we expect the fiscal deficit to clock in at PKR 8.7trn (33% YoY higher), despite the measures taken by the government to improve revenue collection.

Exhibit: Breakdown of total expenditure



Source (s): MOF, AHL Research

Exhibit: Fiscal landscape

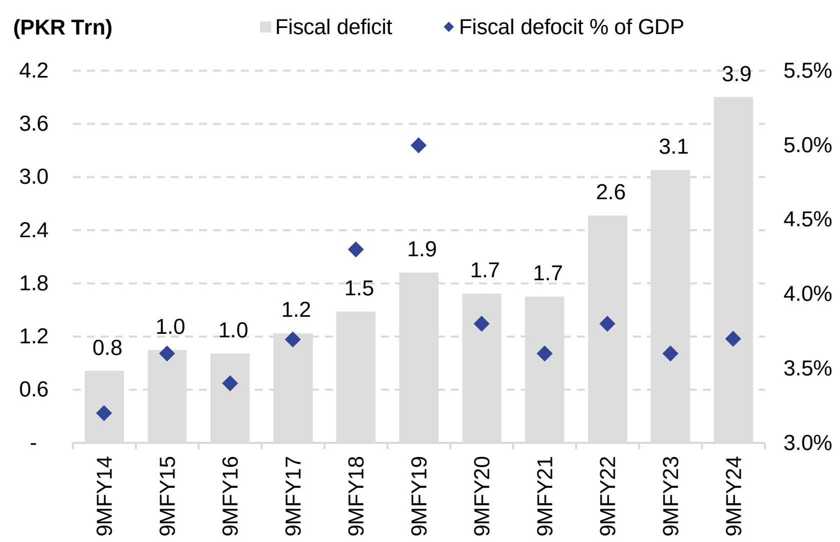


Source (s): MOF, AHL Research

Fiscal performance in 9MFY24

- Pakistan's fiscal balance in the outgoing nine months of FY24 posted a deficit of PKR 3.9trn, 27% YoY higher than the prior year's deficit.
- In terms of the GDP percentage, the deficit settled at 3.7% in 9MFY24 compared to 3.6% recorded in 9MFY23.
- The primary balance during 9MFY24 posted a surplus of PKR 1.6trn (1.5% of GDP) compared to a surplus of PKR 6.7trn witnessed in SPLY (7.9% of GDP).
- Total revenue growth of 41% in 9MFY24 to PKR 9.8trn (9MFY23: PKR 6.9trn) aided the fiscal balance, translating to 9.2% of GDP vs. 8.2% in same period last year.
- Total revenue collected by the FBR marked a 30% YoY growth, clocking-in at PKR 6.71trn compared to PKR 5.16trn in 9MFY23.
- Indirect taxes in 9MFY24 exhibited a 21% YoY growth, amounting to a total of PKR 3.5trn compared to PKR 2.9trn last year.
- Direct taxes jumped +41% YoY to PKR 3.3trn mainly contributing to the overall revenue collection.
- The government collected PKR 2.5trn in non-tax revenues, witnessing a remarkable growth of 91% YoY. This substantial increase was primarily attributed to a significant surge in Petroleum Levy collections which experienced a staggering 99% YoY rise, reaching PKR 720bn.
- Total expenditure went up by 37% YoY to PKR 13.7trn (12.9% of GDP vs. 11.9% of GDP in 9MFY23).
- Further breakup revealed that current expenditure underwent an uptick of 33% YoY of which defense rose by 22% YoY. However, markup payments marked a growth of 54% YoY to PKR 5.5trn.
- Moreover, total PSDP expenditure in 9MFY24 arrived at PKR 1.16trn (14% YoY) with provincial expenditure at PKR 888bn (23% YoY), outdoing federal disbursement of PKR 270bn (-8% YoY).

Exhibit: Fiscal performance in 9Ms



Source (s): MoF, AHL Research

Budget Preview FY25
Proposed revenue measures

Exhibit: Key revenue measures

S. No	Item	Impact (PKR bn)	Probability
1	Imposition of GST or carbon tax on MS and HSD of PKR 40/ltr	691	High
2	Additional taxation on salaried and business income individuals	650	High
3	Increasing FED on tobacco products by 37%	38	Medium
4	Removal of tax and duty for FATA and PATA region	31	Medium
5	Removal of tax exemption on tractors and pesticides	30	High
6	Imposition of pension tax and withdrawal of existing income tax exemptions for pension funds & schemes	25	High
7	Increasing withholding tax on cash withdrawal by non-filers from 0.6% to 0.9%	15	Medium
	Total	**1,480**	
	FBR revenue (FY24e)	9,254	
	FBR revenue (FY25f)	11,251	
	Addition requirements	1,997	
	Nominal growth (15.2% = 11.8% CPI + 3.36% real growth)	1,403	
	New taxation measures required	594	
	Available options	1,480	

Source: AHL Research

Proposed revenue measures

- **Imposition of carbon tax or incremental PDL of PKR 40/ltr:** The IMF has recommended the government to reintroduce GST on petroleum products. However, the government is contemplating increasing the petroleum levy from PKR 60/litr to PKR 100/litr. These measures will enable the government to gather more funds to meet its revenue requirements. The additional PKR 40/ltr is likely to generate PKR 691bn.
- **Additional taxation on salaried and business income individuals :** The government is planning to change the current salary structure as mandated by the IMF, where the highest taxable income limit of salaried person would be lowered to PKR 333,000 from PKR 500,000 per month (35% tax to be charged).
- **FED on Tobacco to be increased by 37%:** With this, the aim is to increase share of FED in the retail price of economy brands and premium brands to 54% and 72.1% respectively. This will result in additional revenue of PKR 38bn.
- **Removal of tax and duty for FATA and PATA region:** The Finance Minister indicated that the government is not considering to extend tax and duty exemptions from Federally Administered Tribal Areas (FATA) and Provincially Administered Tribal Areas (PATA) regions. The withdrawal of tax and duty exemptions will provide a equal level playing field for all the industries. The government will be able to generate PKR 31bn in terms of taxes and duties.
- **Removal of sales tax exemption on tractors and pesticides:** The tractors and pesticides are currently exempted from sales tax. However due to the IMF's condition of withdrawal of exemptions on different sectors, the government is considering charging sales tax on the said products. Removal of the exemption led to additional revenue of PKR 30bn.

Proposed revenue measures

- **Increasing withholding tax on cash withdrawal by non-filers from 0.6% to 0.9%:** At present, the withholding tax is in place on withdrawals above PKR 50,000 in a single day from the bank account of the non-filers. It is proposed to be increased from 0.6% to 0.9% to generate further revenue of PKR in FY25.
- **Imposition of pension tax and withdrawal of existing income tax exemptions for pension funds & schemes:** The government plans to tax the pension of government employees which are more than PKR 1.2mn a year. In addition to this, the government will also revoke income tax exemptions for various pension schemes and funds. These measures will generate additional tax revenue of PKR 25bn every year for the government.

Budget Preview FY25
Budgetary trends

Exhibit: Budgetary Trend*

PKR bn	FY18	FY19	FY20	FY21	FY22	FY23	FY24b	FY24e	FY25b	FY25f
Gross Revenue Receipts	**4,696**	**4,436**	**5,782**	**6,270**	**7,328**	**8,880**	**12,163**	**13,126**	**16,600**	**16,160**
Net Revenue Receipts	**2,479**	**2,038**	**3,278**	**3,528**	**3,739**	**4,656**	**6,887**	**7,758**	**9,408**	**9,635**
Tax Revenue	**4,066**	**4,072**	**4,334**	**5,066**	**6,755**	**7,819**	**9,200**	**10,066**	**13,100**	**12,062**
FBR Taxes	3,842	3,829	3,998	4,764	6,143	7,169	9,200	9,254	12,400	11,251
Non-Tax Revenue	**854**	**606**	**1,784**	**1,505**	**1,185**	**1,711**	**2,963**	**3,059**	**3,500**	**4,098**
Less: Provincial Share	2,217	2,398	2,504	2,742	3,589	4,223	5,276	5,367	7,192	6,525
Total Expenditure	**4,704**	**5,599**	**6,819**	**7,245**	**9,350**	**11,332**	**14,270**	**16,435**	**18,162**	**19,003**
Current Expenditure	3,814	4,804	6,093	6,349	8,452	10,867	13,320	15,500	16,712	17,873
Mark-up Payments	1,500	2,091	2,620	2,750	3,182	5,831	7,303	8,633	9,787	9,885
Defence	1,030	1,147	1,213	1,316	1,412	1,586	1,804	1,800	2,152	2,160
Others	1,284	1,566	2,260	2,283	3,857	3,451	4,213	5,067	4,773	5,828
Development Expenditure & net lending	**890**	**795**	**726**	**789**	**701**	**890**	**950**	**935**	**1,450**	**1,130**
Federal PSDP	576	502	468	441	400	652	950	550	1,000	880
Budget Deficit	**2,260**	**3,445**	**3,376**	**3,403**	**5,260**	**6,521**	**6,924**	**8,677**	**9,304**	**9,368**
% of GDP										
Total Revenue	12.0	10.1	12.2	11.2	11.0	10.5	11.3	12.2	13.4	13.1
FBR Revenue	9.8	8.7	8.4	8.5	9.2	8.5	8.6	8.6	10.0	9.1
Non-Tax Revenue	2.2	1.4	3.8	2.7	1.8	2.0	2.8	2.9	2.8	3.3
Total Expenditure	12.0	12.8	14.3	13.0	14.0	13.4	13.3	15.3	14.7	15.4
Current Expenditure	9.7	11.0	12.8	11.4	12.7	12.8	12.4	14.4	13.5	14.5
Mark-up Payments	3.8	4.8	5.5	4.9	4.8	6.9	6.8	8.0	7.9	8.0
Defence	2.6	2.6	2.6	2.4	2.1	1.9	1.7	1.7	1.7	1.7
Development Expenditure and net lending	3.0	3.0	1.5	1.4	1.1	1.1	0.9	0.9	1.2	0.9
Budget deficit	5.8	7.9	7.1	6.1	7.9	7.7	6.5	8.1	7.5	7.6

Source (s): MoF, AHL Research *Federal only

Budget Preview FY25
PSX proposals – Neutral

Proposed measure	Comment	Probability
Restoration of section 65C of the Income Tax Ordinance so as to rationalize tax rates for companies listed on the stock exchange	The proposal suggests that section 65C of the Income Tax Ordinance be reinstated, which offers all the newly listed companies a 20% tax credit in the year of listing and in the following years if a 25% minimum free float is maintained. Given the corporate tax rate in Pakistan is very high (at 29% + up to 10% super tax) in comparison to other Asian countries (average of 19.80%), this will long-term tax positive measure in the long term and encourage documentation in the economy.	Unlikely
Withdrawal of 10% tax on the value of bonus shares	In the Finance Act 2023, the government amended clause (29) and inserted section 236Z, treating bonus shares as income for shareholders. This mandated every company issuing bonus shares to withhold 10% of the value of the bonus shares. However, with only 4 companies issuing bonus shares in FY24TD compared to 53 companies in FY23, the government could not generate significant revenue. Therefore, it is proposed to abolish the said amendment and inserted section.	Unlikely
Proposal to provide tax relief to foreign investment in the capital market	Tax relief should be provided to foreign investors, by eliminating any tax on capital gains and dividend income, similar to the exemption given to non-resident banking companies investing in debt securities including T-Bills and PIBs.	Unlikely
CGT on all derivatives and future contracts traded on the stock exchange proposed at 5%	A recommendation has been made to subject all derivatives listed on the stock exchange to a 5% tax, in line with the tax rate on future commodity contracts entered by members of the Pakistan Mercantile Exchange. Implementation of this proposal will result revival of derivative segment.	Unlikely
Exemption on intercorporate dividends from taxes under section 59B of the Income Tax Ordinance	As per the proposal, the exemption on intercorporate dividends for companies eligible for group taxation to be restored given the listed companies already paying a corporate taxes at 29%, super tax up to 10% and then pay another 15% on dividend distribution.	Likely

Source (s): AHL Research

Budget Preview FY25
PSX proposals – Neutral

Proposed measure	Comment	Probability
Alignment of CGT on disposal of securities with other asset classes such as immovable property	PSX has proposed the elimination of capital gains tax (CGT) on securities acquired on or before 30th Jun'22. Currently, there is a flat rate of 12.5% for tax filers (30% for non-tax filers), while the CGT on the sale of immovable property acquired before 2012 is 0%. This creates a disparity among different asset classes.	Unlikely
Reinstate tax credits for small investors under section 62 of the Income Tax Ordinance	To promote long-term savings of small savers such as salary-class individuals, it has been proposed to restore tax credits available for individuals for investment in new shares, mutual funds, sukuks, and life insurance policies under section 62 of the Income Tax Ordinance.	Unlikely
PSX proposes promoting real estate sector and REITs structures	A proposal has been made to exempt the transfer of property under REITs from advance tax (sections 236C & 236K). Meanwhile, the subset clause 99A of part I of the second schedule of the ITO provides an exemption from advance tax on profits or gains from the sale of immovable property to any type of REITs. The proposal further seeks to remove the condition of transactions conducted before 30th Jun'23 in the subset clause.	Likely
Elimination of minimum tax on listed companies	The removal of minimum tax will encourage documentation of the economy and reduce downward pressure on the bottom line of listed companies, which are already operating in and following a stringent regulatory environment, and recognizing current and brought forward losses.	Unlikely
Increase tax credit for small and medium enterprises (SME)	To incentivize small and medium enterprises (SMEs) to become listed and be part of the documented economy, the tax burden should be reduced by offering a tax credit of up to 50% for 3 to 4 years of listing, followed by a 20% going forward of the tax payable.	Unlikely

Source (s): AHL Research

Our take:

The KSE-100 is currently trading at a PER of 4.8x (2025) compared to its 5-year average of 6.1x while offering a dividend yield of ~9.5%. Our preferred stocks are OGDC, PPL, MCB, UBL, MEBL, FABL, HBL, BAFL, LUCK, MLCF, FCCL, FFC, HUBC, INDU, PSO, ILP and SYS.

Sectors

Budget Preview FY25
Banks – Neutral

Proposed measure	Impact	Comment	Probability
Penal tax on lower ADR level	Negative	The banking sector's effective tax rate, currently at 49% and including both corporate tax and super tax. Additionally, a penal tax is expected to be re-imposed on banks with an Advance-to-Deposit Ratio (ADR) between 40%-50% and below 40%. To recall, this tax applies to income from government securities, with ADR levels assessed at the end of December. Although this penal tax was exempted in 2023, it is widely anticipated to be reinstated in 2024.	Likely
Increase withholding tax on cash withdrawal from the banks by non-filers	Neutral	At present, the withholding tax is in place on withdrawals above PKR 50,000 in a single day from the bank account of the non-filers. It is proposed to be increased from 0.6% to 0.9% to generate further revenue of PKR 15bn - 20bn in FY25. This will discourage the non-filers from depositing their money in banks.	Likely
Advance tax on foreign payment by non-filers through credit card to increase by 20%.	Neutral	With this implementation, non-filers spendings will reduce.	Likely
Exemption of advance tax on foreign payments by filers via credit cards.	Positive	The removal of advance tax on foreign payments using credit cards will promote documentation and result in higher spending by the filers.	Unlikely

Source (s): Media, AHL Research

Our take on the sector:

The aforementioned measures are likely to have neutral impact on banking sector except for the ADR related tax which is negative. Despite these measures, we believe the current levels at which banks are trading make them a good 'BUY'. Our top picks are UBL, MCB, HBL, FABL, BAFL and MEBL.

Budget Preview FY25
Fertilizer – Neutral

Proposed measure	Impact	Comment	Probability
Reinstatement of tax credit on majority sales to made to the registered individuals	Neutral	The proposal suggests that the government should provide 3% tax credit when 90% of the sales are made to sales tax registered individuals. This will encourage documentation and incentivize sales tax compliance in the fertilizer industry.	Likely
Sales tax on micro-nutrients to be aligned with rates similar to other fertilizers	Positive	The higher GST rate of 18% on this fertilizer product results in higher costs for farmers and makes it commercially unattractive. Therefore, it is proposed that the GST on micro-nutrients be aligned with the rates of other fertilizer products.	Unlikely
Removal of tax exemption on tractors and pesticides	Neutral to Negative	At present tractors and pesticides have zero-rated sales tax. In the event of the imposition of sales tax, the manufacturers and distributors of tractors and pesticides will pass on the burden of taxation to final consumers by increasing in the selling price. Subsequently, this will increase the cost of agriculture/farming.	Likely
Exemption of sales tax on the import of DAP	Neutral	Currently, imported DAP is subject to a 5% GST, which prevents importers from adjusting their input sales tax of 8%. As a result, this tax becomes part of the cost of importing DAP, leading to higher DAP prices. Therefore, it is proposed that the input GST at the import stage be exempted, which will improve the trading margins of DAP importing fertilizer companies and make DAP available at a reasonable price in the market..	Unlikely

Source (s): Media, AHL Research

Our take on the sector:

The offtake of the fertilizer sector is expected to remain stable due to the government's focus on food security and agriculture in the country. Additionally, we expect domestic manufacturers to effectively pass on the impact of any increase in costs (such as gas price hikes), which will keep the sector's profitability intact. Moreover, SIFC is working on initiatives to promote corporate farming and attract investments in agriculture. Our top pick is FFC.

Budget Preview FY25
E&Ps & OGMCs – Neutral

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Proposed measure	Impact	Comment	Probability
E&P: Allocation of funds to E&P companies	Positive	The proposal seeks the allocation of funds in terms of tariff differential subsidy for FY25 with the purpose of adjusting total revenue shortfall of Sui companies. In the listed space, this will facilitate SNGP, SSGC, OGDC and PPL in terms of better cash flows.	Unlikely
OGMCs: Imposition of levy/carbon tax of PKR 40/ltr	Neutral	The IMF has requested that the government reintroduce GST on petroleum products. In response, the government is considering imposing a carbon tax on petroleum products to secure cheaper loans and grants from multilateral institutions, and/or increasing the petroleum levy from PKR 60/litre to PKR 100/litre. These measures will enable the government to gather more funds to meet its revenue requirements.	Likely
Reduction in minimum tax rate from 0.50% to 0.25%	Positive	The current tax regime is adversely effecting company's fixed margins. If the minimum tax rate is reduced to 0.25%, then this will ease off some of the burden and allow OMCs to maintain margins.	Unlikely

Source (s): Media, AHL Research

Our take on the sector:

E&P: The resolution of gas circular debt will improve the dividend pay out ability of companies amid improved cash flows for OGDC and PPL. Regular gas price revisions will significantly enhance cash earnings. Additionally, the potential sale of the Reko Diq stake could further augment the liquidity of OGDC and PPL. Our top picks are OGDC and PPL.

OGMCs: Resolution of circular debt will improve PSO's cash flow position and dividend pay out. Whereas, gas utilities are set to benefit from the revision in WACC. Our top pick is PSO.

Budget Preview FY25

Cement – Neutral to positive

Proposed measure	Impact	Comment	Probability
PKR 1,000bn allocation for PSDP against target of PKR 950bn last year	Positive	Astonishingly, public spending development project (PSDP) has been proposed at PKR 1,000bn, given the tight fiscal space of the incumbent government. Additionally, no new unapproved development projects will be included in the PSDP. It is pertinent to note that although a target of PKR 950bn was set last year and PKR 507bn has been authorized till Apr'24, actual expenditure arrived at PKR 353bn.	Likely
The Planning Ministry is also proposing an allocation through Public Private Partnership	Positive	Cement demand is expected to be supported, amid the approval of qualified projects under the Public-Private Partnership	Likely
Reduction in FED	Neutral	The imposition of FED has pushed the price of cement to an all time high level, which has dented the construction demand in the economy. Therefore, it has been suggested to reduce the price of FED. However, we believe government would be reluctant to consider this proposal given the dire fiscal space.	Unlikely

Source (s): Media, AHL Research

Our take on the sector:

Given the absence of a price war among companies and inflation on a downward trajectory, which will subsequently lead to monetary easing, we anticipate an increase in demand for construction activities positively impacting the profitability of the cement sector. Additionally, use of local coal would aid in reducing the cost of manufacturing, keeping margins at elevated levels. Furthermore, cement companies are trading at attractive valuations. Our top picks are LUCK, MLCF, and FCCL.

Budget Preview FY25
Power – Neutral

Proposed measure	Impact	Comment	Probability
Increase in Power subsidy	Neutral	Despite the massive increase in power tariff, a colossal amount of PKR 1.2trn in subsidy has been sought by the Ministry of Energy for FY25.	Unlikely
Increasing advance income tax on non-tax filers	Neutral	It is proposed to increase advance income tax on non-tax filers up to 30% on electricity bills. Currently, the non-tax filers pay advance tax of 12% which is proposed to increase to 30% for domestic consumers with monthly bills exceeding PKR 200,000.	Likely

Source (s): Media, AHL Research

Our take on the sector:

With the condition of the IMF to keep the stock of circular debt for power at PKR 2.3trn, the government is expected to timely increase the electricity tariff, which will improve the cash flow position for the sector. Moreover, we believe the cash flow position of CPEC-based IPPs will be better than others. Our top pick is HUBC.

Budget Preview FY25
Auto Assemblers – Neutral

Proposed measure	Impact	Comment	Probability
Annual advance tax for Vehicles of 2000cc and Above (non-filer)	Neutral	Currently , the FED of PKR 20,000 is charged on Vehicles of 2000cc and above. Its is proposed to replace this FED with advance tax of PKR 500,000 for the non-filers.	Likely
Advance Tax on Purchase of Vehicles by Non-Filers	Negative	Currently, FED rates of 6.00%, 8.00%, and 10.00% are applied to vehicles with engine capacities of 2001cc-2500cc, 2501cc-3000cc, and 3001cc and above, respectively. The proposed plan suggests imposing an advance tax of 24.00% across all categories.	Unlikely
Tax holiday of 7 years on exports of all kinds of vehicle	Positive	The proposal aims to incentivize the auto assemblers to commence export or increase existing exports of all assembled/manufactured vehicles including 2 & 3-wheelers and EV vehicles. With this, the assemblers/manufacturers will focus on exports, resulting in improvement in earnings.	Unlikely
Withdrawal of tax exemption on tractors	Neutral	The government is considering the withdrawal of the zero-rated sales tax regime on tractors, given IMF's recommendation to end the exemptions in various sectors. The tractor manufacturers will pass on the sales tax impact via a hike in selling price.	Likely

Source (s): Media, AHL Research

Our take on the sector:

Automobile sector volumes are anticipated to see a long-awaited recovery post-economic stability and decline in interest rates, with hybrid electric vehicles (HEVs) likely to gain prominence due to their fuel efficiency. Our top pick is INDU.

Budget Preview FY25
Engineering – Neutral to positive

Proposed measure	Impact	Comment	Probability
PKR 1,000bn allocation for PSDP against target of PKR 950bn last year	Neutral	Astonishingly, public spending development project (PSDP) has been proposed at PKR 1,000bn, given the tight fiscal space of the incumbent government. Additionally, no new unapproved development projects will be included in the PSDP. It is pertinent to note that although a target of PKR 950 bn was set last year and PKR 507bn has been authorized till Apr'24, actual expenditure arrived at PKR 353bn.	Likely
Discontinuation of exemption on import stage sales tax for the FATA / PATA region	Positive	Unregistered steel producers from the FATA/PATA region persist in manipulating the FBR to evade taxes and flood the market with low-cost steel rebars. This unfair practice has inflicted significant damage on the legitimate rebar and flat steel industry. Consequently, it is imperative to cease the GST exemption for this region to prevent revenue losses from tax evasion and safeguard the formal steel industry operating outside the area.	Likely
The Planning Ministry is also proposing an allocation through Public Private Partnership	Positive	Steel demand is expected to be supported, amid the approval of qualified projects under the Public-Private Partnership.	Likely
Reduction in minimum turnover tax from 1.25% to 0.5%	Positive	To provide cash flow relief to the steel sector during this period of economic difficulty, the turnover tax for manufacturers and downstream retailers/traders must be reduced from the current 1.25% to 0.5%.	Unlikely

Source (s): Media, AHL Research

Our take on the sector:

The sector is expected to receive a much-needed boost due to the easing of import restrictions and a stable exchange rate, as it heavily relies on imported raw materials. Additionally, monetary easing is anticipated amid falling inflation, which can enhance the sector's bottom line. However, it is crucial to remain vigilant about any further devaluation of the PKR against the greenback, as well as potential gas and electricity tariffs increases, which could continue to exert pressure on the sector.

Budget Preview FY25
Textile – Neutral

Proposed measure	Impact	Comment	Probability
Restoration of zero rating of sales tax	Positive	Reviving the zero-rated facility for export-oriented businesses will lower operating costs by enabling companies to claim tax rebates on their input expenses. This measure will alleviate the financial challenges faced by exporters and help prevent working capital shortages.	Unlikely
Allocation of PKR 250bn for the outstanding tax rebates	Positive	A total of PKR 145bn in sales tax, PKR 25bn in duty drawbacks, and PKR 40bn in income tax and income tax credits have remained outstanding for several years. Additionally, PKR 40bn under the textile policy for duty drawback taxes, technology upgradation funds, and markup support remain unpaid. Consequently, a total allocation of PKR 250bn is needed for the sector.	Unlikely
Tariff rationalization	Positive	The energy tariffs rates should be rationalized , ensuring that the burden of subsidies provided to other sectors does not fall on textile exporters.	Unlikely

Source (s): Media, AHL Research

Our take on the sector:

Rising energy tariffs are likely to impact production and squeeze profit margins. However, the revival in the economies of North America and Europe is expected to revive order volumes. Our top pick is ILP.

Budget Preview FY25
Technology & Communication – Neutral

Proposed measure	Impact	Comment	Probability
Elimination of WHT on telecom services	Positive	The abolishment of withholding tax (which is 15% at present) will improve affordability of mobile services in the country and increase mobile network operator's revenues.	Unlikely
Minimum tax rate on Salary of Individual	Positive	Provided that maximum rate of tax applicable on salary of an individual shall not exceed 5% if such individual is receiving salary from a person registered with PSEB and P@SHA. This will encourage work force of the country to work in IT sector.	Unlikely

Source (s): Media, AHL Research

Our take on the sector:

Despite the global economic slowdown, Pakistan's technology sector has shown remarkable growth, underscoring its significant export potential. As of 10MFY24, the sector has achieved exports worth USD 2.6bn and is projected to reach USD 3.2bn by the end of the fiscal year. Government support and tax exemptions have played a crucial role in this growth. Given Pakistan's substantial young population, the tech sector is well positioned to not only enhance foreign exchange reserves but also to drive employment opportunities. Our top pick is SYS.

Budget Preview FY25
Others – Neutral

Proposed measure	Impact	Comment	Probability
Pharmaceuticals: Imposition of 18% GST on medicines	Neutral	In the event of the imposition of GST, pharmaceutical companies will pass on the impact by raising medicine prices for the final consumer.	Likely
Reduction of 5% custom duty on raw material imports	Positive	The custom duty reduction will improve the gross margins of the pharmaceutical sector, since the cost of importing pharma ingredients will decline.	Unlikely
Real Estate: Increase in advance tax on purchase of immovable property by non-filers	Neutral	For non-filers, the proposal suggests that the advance income tax should be increased to 12% from 10.5% on Property value between PKR 50-100mn for non-filers.	Unlikely
Exemption of CGT on sale of property held for more than 4 years	Neutral	The proposal advocates abolishing the capital gain tax on the sale of property held for 4 – 6 years for individuals who have disclosed the property post-acquisition.	Unlikely
Tobacco: Increase in FED on Tobacco Products	Negative	The proposal suggests increasing FED on tobacco products by 37%. With this, the aim is to increase share of FED in the retail price of economy brands and premium brands to 54% and 72% respectively. Tobacco companies are likely to pass on the impact by raising the price of manufactured cigarettes. Tobacco has inelastic demand, this measure will be able to generate additional revenue for the government.	Likely

Source (s): Media, AHL Research

Others – Neutral

Proposed measure	Impact	Comment	Probability
Beverages: Increase in FED on Sugary drinks/juices	Neutral	The sweetened beverages industry includes sodas, juices, energy drinks, flavored milk, and other similar beverages. If the proposal materializes, then it will be passed on to end consumers.	Unlikely
Insurance: Collaboration of Govt. with insurance companies to offer schemes under the umbrella of BISP	Positive	The government is planning to initiate inclusive schemes related to Benazir Income Support Program by collaborating with insurance companies. This initiative will support the expansion of reach and accessibility of micro-insurance/inclusive to the masses, boding well for the sector.	Likely

Source (s): Media, AHL Research

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Arif Habib Limited (AHL) uses three rating categories, depending upon return form current market price, with Target period as Dec 2024 for Target Price. In addition, return excludes all type of taxes. For more details, kindly refer the following table;

Rating	Description
BUY	Upside* of subject security(ies) is more than +15% from last closing of market price(s)
HOLD	Upside* of subject security(ies) is between -15% and +15% from last closing of market price(s)
SELL	Upside* of subject security(ies) is less than -15% from last closing of market price(s)

Equity Valuation Methodology

AHL Research uses the following valuation technique(s) to arrive at the period end target prices;

- Discounted Cash Flow (DCF)
- Dividend Discount Model (DDM)
- Sum of the Parts (SoTP)
- Justified Price to Book (JPTB)
- Reserved Base Valuation (RBV)

Risks: The following risks may potentially impact our valuations of subject security (ies);

- Market risk
- Interest Rate Risk
- Exchange Rate (Currency) Risk

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Disclosure required under Research Analyst Regulations, 2015:

In order to avoid any conflict of interest, we hereby disclosed that; Arif Habib Limited (AHL) has shareholding in NBP, BOP, MLCF and FCCL.